PUBLIC VERSION

INDIA -- MEASURES AFFECTING THE AUTOMOTIVE SECTOR

(WT/DS146-175)

FIRST SUBMISSION OF
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I. INTRODUCTION

1. In the early 1990's, faced with a pent-up consumer demand for automobiles, India began to liberalize foreign investment in its motor vehicle manufacturing sector. A number of foreign car companies took advantage of this opening and entered into manufacturing joint ventures with Indian firms.

2. This welcome new foreign investment policy was, unfortunately, undermined by the implementation of discriminatory trade and investment measures. In December of 1997, the Director General of Foreign Trade issued Public Notice No. 60 ((PN)/97-02) of the Indian Ministry of Commerce ("Public Notice No. 60"), a policy with the force of law under India's foreign trade laws, that took advantage of the following two facts: first, these joint ventures import automotive parts into India; and second, automotive components and kits in "completely knocked down" ("CKD") or "semi-knocked down" ("SKD") form are subject to India's restrictive import licensing regime.

3. Under Public Notice No. 60, in order to obtain the necessary import licenses, companies manufacturing cars in India must do the following: (i) use local content for a specified percentage of their production (50% in the first three years, 70% by the end of five years); (ii) meet certain export- and trade-balancing requirements; and (iii) if they are joint ventures involving majority foreign ownership, invest at least $50 million of equity. Public Notice No. 60 further dictates that these manufacturing firms sign a standard-form memorandum of understanding ("MOU") with the Government of India that elaborates on these requirements. All or virtually all firms that manufacture passenger cars in India are bound by Public Notice No. 60 and have signed MOU's. Exhibit US-1 is a copy of Public Notice No. 60 and its appendix, the standard-form MOU.

4. The local content (or "indigenisation") requirement in these measures plainly discriminates against imported automotive parts and components of *any* kind (not just SKD/CKD kits/components) and from *any* non-Indian origin; it does so by preventing those parts and components from constituting more than 50% (at first) or more than 30% (in later years) of an automobile manufactured in India. The trade- and export-balancing requirement is also discriminatory; it discriminates against imported SKD/CKD kits or components by imposing an obligation on their users and purchasers (namely, the obligation to export an equal value of automobiles or automotive parts) that it does not impose on users and purchasers of like Indian kits or components.

5. But these requirements do more than just discriminate; they also restrict imports outright. The trade balancing requirement limits any car manufacturer's imports of SKD/CKD kits/components to an amount that is correlated to the manufacturer's exports of automobiles and their components, and the indigenisation requirement restricts or even prohibits such imports by any manufacturer who has not met the 50% or 70% local content quotas. This is not just preferential treatment for domestic goods in the local marketplace at the expense of their imported competitors; it is keeping the competition out altogether.

6. The United States had hoped not to have to pursue this dispute. In the first place, India put these requirements into place almost three years after the WTO Agreement entered into force; in the Uruguay Round, however, all Members had agreed not to introduce any more such measures. Second, the import licenses that India requires for SKD/CKD kits (and through which it currently enforces the obligations in Public Notice No. 60 and the MOU's) are one piece of a complex regime of quantitative restrictions that India has applied to imports for many years. In a previous dispute, a panel and the Appellate Body concluded that India no longer has a balance-of-payments justification for many of these restrictions, including the licenses imposed on the importation of SKD/CKD kits. India is clearly committed to eliminating those licensing restrictions by April 1 of this year, and the United States applauds the efforts that India is undertaking in that connection.

7. But, surprisingly, neither of these facts has resolved this dispute. India intends to maintain and to continue enforcing the requirements of Public Notice No. 60 and the MOU's even after its import licensing regime ends. The present dispute, therefore, concerns not the import licenses themselves; maintaining them beyond April 1 would in any case be inconsistent with India's existing obligation to remove them. Instead, this dispute concerns discriminatory, trade-restricting conditions that India exacts from investors in the motor vehicle manufacturing sector -- and that it intends to continue to exact.

8. The United States contends that the local content and trade balancing requirements in Public Notice No. 60 and the MOU's, together with the Indian domestic legislation under which they have come into force, are inconsistent with the obligations of India under the General Agreement on Tariffs and Trade 1994 ("GATT 1994") and the Agreement on Trade-Related Investment Measures ("TRIMs Agreement"). The United States respectfully requests this Panel to make findings to this effect, and to recommend that India bring all such measures into conformity with its obligations.

II. PROCEDURAL BACKGROUND

9. On 6 October 1998, the European Communities requested consultations with India pursuant to Article 4 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU"), Article XXII:1 of the GATT 1994 and Article 8 of the TRIMs Agreement, concerning certain measures affecting the automotive sector.[1] The request was circulated on 12 October 1998. The European Communities and India consulted on these measures in Geneva on 2 December 1998. The United States and Japan participated in the consultations as interested third parties under DSU Article 4.11.

10. On 2 June 1999, the United States requested consultations with India pursuant to DSU Articles 1 and 4, Article XXII:1 of the GATT 1994, and Article 8 of the TRIMs Agreement (to

[1] WT/DS146/1 & Corr. 1.

the extent it incorporates by reference Article XXII of the GATT 1994), regarding certain measures affecting trade and investment in the motor vehicle sector.[2] The request was circulated on 7 June 1999. The United States and India consulted on these measures in Geneva on 20 July 1999. The European Communities and Japan participated as interested third parties under DSU Article 4.11. In addition, on 30 July 1999, the United States posed certain additional questions to India in writing; India replied on 13 July 2000.

11. Although these consultations and India's answers to the United States' questions provided some helpful clarifications, they failed to settle the dispute.

12. On 15 May 2000, the United States requested that the WTO Dispute Settlement Body ("DSB") establish a panel to examine this dispute.[3] The DSB established the panel on 27 July 2000 with standard terms of reference.[4]

13. On 12 October 2000, the European Communities also requested that the DSB establish a panel to examine this dispute.[5] At its meeting on 17 November 2000, the DSB established the panel on the EC complaint with standard terms of reference. The DSB further agreed that, in accordance with DSU Article 9.1, the panel established on 27 July 2000 to examine the U.S. complaint should also examine the complaint by the European Communities.[6] The terms of reference of the panel are therefore as follows:

> To examine, in the light of the relevant provisions of the covered agreements cited by the United States in WT/DS/175/4 and by the European Communities in WT/DS146/4, the matters referred to the DSB by the United States and the European Communities in those documents and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements.[7]

III. FACTUAL BACKGROUND

14. The United States challenges the indigenisation requirement and the trade balancing requirement that the Government of Indian imposes through Public Notice No. 60 and the MOU's signed by individual manufacturing companies. Because these measures in their present form are

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[2] WT/DS175/1. A copy of the U.S. consultation request is attached as Exhibit US-2.

[3] WT/DS175/4. A copy of the U.S. panel request is attached as Exhibit US-3.

[4] *Dispute Settlement Body: Minutes of Meeting Held on 27 July 2000*, WT/DSB/M/86, para. 58.

[5] WT/DS146/4.

[6] *Dispute Settlement Body: Minutes of the Meeting Held on 17 November 2000*, WT/DSB/M/92, paras. 49-50.

[7] *India – Measures Affecting the Automotive Sector: Constitution of the Panel Established at the Requests of the United States and the European Communities: Note by the Secretariat*, WT/DS146/5, WT/DS175/5, 30 November 2000, para. 2.

linked to (and in fact currently enforced through) the import licensing regime that India applies to motor vehicles and to automotive parts and components, subpart A of this factual background begins with a description of that licensing regime. Subpart A then describes the requirements in Public Notice No. 60 and the MOU's; the requirements are essentially the same in both, although the MOU's do place a few additional obligations on signatories. Subpart A also explains enforcement mechanisms under Indian law for these measures (one of which is the possibility of withholding import licenses), and describes India's success in having manufacturers sign the MOU's.

15. Subpart B provides, for the sake of context, a brief overview of India's broader investment policy in the automotive sector: liberalized permission to invest in the manufacture of finished vehicles, accompanied by restrictive trade measures to shelter the domestic automotive parts and components industry.

16. Subpart C describes the relationship between this dispute and the dispute in *India - Quantitative Restrictions on Imports of Agricultural, Textile and Industrial Products*. In particular, subpart C describes how the rejection in that dispute of India's asserted balance-of-payments defense led to an agreement between India and the United States that should bring import licensing of automotive parts and components to an end; but it also describes India's regrettable intention to continue enforcing its trade-restricting indigenisation and trade balancing requirements nonetheless.

A. Public Notice No. 60 and the MOU's: Trade Restrictions in the Automotive Sector

17. On 12 December 1997, the Director General of Foreign Trade issued Public Notice No. 60, which was published in the *Gazette of India Extraordinary*.[8] The subject of Public Notice No. 60 is the Export and Import Policy 1997-2002, and in particular the policy relating to the import of CKD/SKD kits/components by car manufacturing companies under MOU's to be signed with the Government of India. Although the notice appears to address only joint ventures, as opposed to wholly-owned enterprises, the Government of India has confirmed that no such distinction is made: "The requirements are applicable uniformly to both Indian companies as well as to joint venture companies."[9]

1. The Background to Public Notice No. 60: Indian Import Licensing of Motor Vehicles and Motor Vehicle Kits/Components

18. In paragraph 2, Public Notice No. 60 notes that the import of components for motor vehicles in CKD (*i.e.*, completely knocked-down) and SKD (*i.e.*, semi-knocked-down) forms is "restricted" for import under the *Export and Import Policy 1997-2002* ("Exim Policy"). The

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[8] Exhibit US-1.

[9] *Replies by India to Questions Posed by Japan*, G/TRIMS/W/15, circulated 30 October 1998, answer to question 16; Exhibit US-5.

Exim Policy is the basic document of the Indian import and export regime, and it prescribes eligibility requirements and other conditions for importing and exporting.[10]

19. Paragraph 4.5 of the Exim Policy defines a category of "restricted" goods as follows: "Any goods, the export or import of which is restricted under ITC (HS) may be exported or imported only in accordance with a license issued in this behalf."[11] India has clarified that "import of any restricted item is possible either through an import licence or in accordance with any Public Notice issued for this purpose."[12]

20. At the time Public Notice No. 60 was issued, 90 tariff line items in Chapter 87 ("vehicles other than railway or tramway rolling-stock, and parts and accessories thereof") of India's tariff schedule were "restricted" and therefore subject to import licensing requirements; India claimed a balance-of-payments justification for those requirements.[13] For example, tariff heading 870321.01 ("Other vehicles, with spark-ignition internal combustion reciprocating piston engine; Of a cylinder capacity not exceeding 1,000 cc; Motor car, new, assembled") is marked in the ITC (HS) Classifications as "Restricted: Not permitted to be imported except against a licence or in accordance with a Public Notice issued in this behalf." Tariff heading 870321.04 ("... Complete units not assembled") is restricted in the same manner; and so on.[14] At present, these import licensing requirements still apply to approximately 75 tariff line items in Chapter 87.[15] India

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[10] A copy of chapters 1 through 5 of the current Exim Policy, as amended through 13 October 2000 (concerning the prescribed procedures, conditions and eligibility requirements for imports), is attached as Exhibit US-4. A copy of the complete Exim Policy, as amended through 31 March 2000, was deposited by India with the WTO Secretariat on 10 November 2000. *Agreement on Import Licensing Procedures: Notification under Articles 1.4(a) and 5 of the Agreement*, G/LIC/N/1/IND/3, G/LIC/N/2/IND/3, circulated 13 December 2000. The chapters included in Exhibit US-4 have been downloaded from the Indian Government website to which that notification refers: <http://www.nic.in/eximpol>.

[11] The reference in paragraph 4.5 to "ITC (HS)" is a reference to India's *ITC (HS) Classifications*. This document implements the Exim Policy at a product-specific level, by relating the rules of the Exim Policy to the 8-digit tariff headings set forth in the Harmonized System of commodity classification, as adopted by India. For each product listed, the book indicates, *inter alia*, the applicable restriction policy (or "free" in the case of items not requiring a license under the Exim Policy). Sample pages of the ITC (HS) Classification are attached as Exhibit US-6.

[12] *Replies to Questionnaire on Import Licensing Procedures*, G/LIC/N/3/IND/4, circulated 4 December 2000, para. 5; Exhibit US-7. This document also provides an overview of India's import regime and was submitted to the WTO pursuant to Article 7.3 of the Agreement on Import Licensing Procedures.

[13] *Notification under Paragraph 9 of the Understanding on the Balance-of-Payments Provisions of the General Agreement on Tariffs and Trade 1994*, WT/BOP/N/24, 19 May 1997, Annex I, Part B, Sl. Nos. 2392-2481. A copy of the relevant pages of this Notification is attached as Exhibit US-8.

[14] Exhibit US-6.

[15] *See Indian Notification to the United States under the U.S. – India BOP Settlement: Products To be Freed by 1 April 2001*, Exhibit US-21, which contains a list of items still restricted as of April 1, 2000. The restricted motor vehicle tariff lines are found at Continuous Sl. Nos. 603-677. (The Continuous Sl. Nos. in the right-most column are unique to Exhibit US-21; the Sl. Nos. in the left-most column, however, correspond to the Sl. Nos. in India's 1997 notification to the Committee on Balance-of-Payments Restrictions, Exhibit US-8.)

applies those licensing requirements both to finished vehicles as such and to SKD/CKD kits/components for such vehicles.[16]

21. Consequently, when Public Notice No. 60 was issued, no one was permitted to import finished motor vehicles, or kits and components in CKD/SKD form for such vehicles, into India without a license; in large part (for 75 out of 90 tariff line items) that remains true today.

2. Public Notice No. 60 Establishes the Requirements for Getting Import Licenses

22. Paragraph 2 of Public Notice No. 60 goes on to explain how such import licenses can be obtained. It provides that such licenses shall be issued only to automobile manufacturing companies on the basis of an MOU to be signed by those companies with the Indian Government.

23. Subparagraphs 3(i) through (iv) of Public Notice No. 60 set out four requirements which an MOU must impose on the manufacturing company:

(i) Establishment of actual production facilities for manufacture of cars, and not for mere assembly.

(ii) A minimum of foreign equity of US $ 50 million to be brought in by the foreign partner within the first three years of the start of operations, if the firm is a joint venture that involves majority foreign equity ownership.[17]

(iii) Indigenisation (*i.e.*, local content) of components up to a minimum level of 50% in the third year or earlier from the date of first import consignment of CKD/SKD kits/components, and 70% in the fifth year or earlier.

(iv) A broad neutralization of foreign exchange over the entire period of the MOU in terms of balancing between the actual CIF value of imports of CKD/SKD kits/components and the FOB value of exports of cars and auto components over

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[16] *See* ITC (HS) Import Licensing Note on SKD/CKD, Exhibit US-10, *and* India's Answers to Questions by the United States, 13 July 2000, answer to Supplemental Question 2; Exhibit US-11. According to the Government of India, the importation of automotive parts and components other than kits/components in CKD or SKD form does not require a license, and the distinction between "parts and components" on the one hand, and "kits/components in CKD or SKD form" on the other hand, can be found in various sources, including Rule 2(a) of the General Rules for the Interpretation of the Harmonized System; and Public Notice No. 3, dated 6 January 1998, which was issued by the Delhi Customs House and was based on Indian Ministry of Finance, Department of Revenue circular F.No.528/128/97-Cus(TU) of 5 December 1997. A copy of Public Notice No. 3 is attached as Exhibit US-12.

[17] Paragraph 3(ii) also provides that this condition applies to new joint venture companies only. In response to a question from Japan, India stated that "this condition has been imposed on new joint venture companies because the existing companies have already invested more than their minimum stipulation." *Replies by India to Questions Posed by Japan*, G/TRIMS/W/15, circulated 30 October 1998, answer to question 18; Exhibit US-5.

that period. While a firm that signs an MOU has an export obligation equivalent to the total CIF value of the imports made by the firm over the period of the MOU, there is a two-year moratorium during which the firm does not need to fulfill that commitment. The period of export obligation therefore begins from the third year of commencement of production. However, imports made during the moratorium count towards the firm's total export obligation under the MOU.

24. Indian statements have elaborated on these requirements. With respect to indigenisation, the Director-General of Foreign Trade has confirmed that, "for purposes of indigenisation, *use of local materials alone will be taken into account* and there was no escape from that. For instance, if a vendor chosen by a manufacturer imports components to turn out an essential item like a gear box, the indigenisation level will be calculated on the quantum of local materials used. In other words, local value added will be the determining factor for arriving at the indigenisation level. If, however, no materials have been procured locally by a vendor, it will be construed as having failed to fulfill the norm."[18] In other words, Public Notice No. 60 imposes a straightforward preference for domestic over imported goods.

25. With respect to the export- and trade-balancing requirement in paragraph 3(iv), India has said that a firm must balance not only the value of CKD/SKD kits and components that the firm imports itself, but also the value of the firm's purchases in India of components or kits imported by others.[19] Thus, a company that chooses imported goods rather than domestic is penalized for that choice: it must manage to export an equivalent amount of autos or auto components, which it would not have to do if it had chosen to use or buy local goods instead.

3. The Actual MOU's Impose Requirements Beyond Those in Public Notice No. 60

26. Paragraph 8 of Public Notice No. 60 requires MOU's to be signed in a standard format, which is appended to the Notice.[20] The MOU is to be signed by the Government of India acting through the Director General of Foreign Trade and by the managing director of the manufacturing company on its behalf.

27. Paragraph III of the standard MOU format reconfirms each of the requirements of Public Notice No. 60 described in paragraph 23 above. The requirement to establish actual manufacturing facilities, and not mere assembly facilities, appears in MOU paragraph III, clause (iii); the $50 million equity requirement appears in MOU paragraph III, clause (ii); the

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[18] "DGFT Open to Relaxation of Indigenisation Norms for Cars," *The Financial Express*, 12 January 1998 (emphasis added), attached as Exhibit US-13. *See also* India's Replies to Questions Posed by the United States, 10 May 1999, answer to question 6: "[redacted]" Exhibit US-14.

[19] *Replies by India to Question Posed by Japan*, G/TRIMS/W/15, dated 10 September 1998 and circulated 30 October 1998, answer to question 23; Exhibit US-5.

[20] A copy of that standard format is included as part of Exhibit US-1.

indigenisation obligation appears in MOU paragraph III, clause (iv); and the trade balancing obligation appears in MOU paragraph III, clause (vi).

28. However, paragraph III of the standard MOU format also imposes additional requirements on the manufacturing firm. First, clause (i) provides that the foreign partner's equity share must be in a specified amount over a specified time frame, and must be in a freely convertible currency; in other words, it is not sufficient to reinvest rupees earned within India. Second, several clauses call for the firm to make projections for future years; for example, clause (iv) calls for the firm to state its intended level of indigenisation year by year, and clause (vi) calls for the firm to indicate the total value in rupees and dollars, year by year, of the cars and auto components that the firm intends to export.

29. The most significant additional requirement, however, comes at the end of clause (iv). That clause provides that the firm "shall aggressively pursue and achieve as soon as possible the development of the local supply base and increased local content". This requirement, which does not figure in the main body of Public Notice No. 60, emphasizes in the most straightforward terms the intentions that underlie the MOU scheme: to induce manufacturing firms to abandon imported goods and to favor domestic goods instead.

4. Mechanisms for Enforcing the Requirements: Licensing Denials and Other Penalties

30. Paragraph 4 of Public Notice No. 60 provides that the MOU scheme is to be enforced through the import licensing mechanism. Paragraph 5 provides for MOU signatories to submit annual reports and for Indian officials to conduct an annual review of signatories' progress towards meeting their MOU obligations.

31. These provisions should be read in conjunction with the final three sentences of paragraph 3(iii) and one sentence in paragraph 3(iv). Paragraph 3(iii) indicates that once an MOU signing firm has reached an indigenisation level of 70%, there will be no need for further import licenses, and that consequently, as and when firms achieve 70% indigenisation, they go outside the ambit of the MOU entirely. By implication, licenses will be withheld if the targets are not met. Indeed, India has confirmed that [redacted].[21]

32. The final sentence of paragraph 3(iii) also makes clear that the trade balancing obligation of paragraph 3(iv) remains in place independently of the indigenisation obligation: "However, they [*i.e.*, firms that have achieved 70% indigenisation] will discharge the export obligation corresponding to the import made by them till that time." Paragraph (iv) then provides that "From 4th year onwards [*i.e.*, after the export obligation has begun to apply] the value of imports of CKD/SKD may be regulated with reference to the export obligation fulfilled in the previous years as per the MOU." The Government of India confirmed this point in its reply to a question

[21] India's Answers to Questions by the United States, 13 July 2000, answer to question 5, Exhibit US-11 (underlining in original, other emphasis added).

posed by the Government of Japan: "CKD/SKD kits imports would be allowed with reference to the extent of export obligation fulfilled in the previous year. ... If the company has met the 70% indigenisation level and has not even started exports, its imports could be limited under the provisions of the notification."[22]

33. In short, the purpose of these provisions is clear: failure to abide by either of these requirements entails the denial of import licenses.

34. India has also said, however, that [redacted].[23]

35. India is referring to the *Foreign Trade (Development and Regulation) Act 1992* (the "FTDR Act"), which empowers the Indian Central Government to develop, announce and regulate Indian trade policy.[24] For instance, section 5 of the FTDR Act authorizes the Indian Central Government to formulate and announce by notification in the Official Gazette the Exim Policy. The FTDR Act also permits the Government to regulate what can be imported, and to take enforcement measures. For example:

(a) Section 3(2) of the FTDR Act authorizes the Indian Government to prohibit, restrict or otherwise regulate the import or export of goods. Under section 3(3) of the FTDR Act, all goods to which any Order under section 3(2) applies are deemed to be goods the import or export of which has been prohibited under section 11 of the Customs Act, 1962, and all provisions of that Act have effect accordingly. Such goods are therefore subject to confiscation under section 111 of the Customs Act.[25]

(b) Section 7 of the FTDR Act prohibits imports or exports except by persons who have been granted an Importer-Exporter Code Number ("IEC Number") by the Director General of Foreign Trade. Pursuant to Section 8 of the FTDR Act, the Director General of Foreign Trade may cancel the IEC Number of any person who has contravened customs laws or has committed any other economic offense under others laws specified by the Indian Government.

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[22] *Replies by India to Questions Posed by Japan*, G/TRIMS/W/15, circulated 30 October 1998, answer to question 24; Exhibit US-5. In answer to question 20, India also declared that "each of the three obligations under the MOU continues until it is met with fully. Once *all* the obligations are met, the company goes out of the MOU completely." (Emphasis added.)

[23] India's Answers to Questions by the United States, 13 July 2000, answer to supplemental question 3; Exhibit US-11.

[24] A copy of the FTDR Act is attached as Exhibit US-16.

[25] Section 11 of the Customs Act 1962 provides that if the Central Government is satisfied that it is necessary so to do for any of 22 listed purposes, it may, by notification in the Official Gazette, prohibit (absolutely or subject to conditions) the import or export of any particular goods. Under Section 111 of the Customs Act 1962, goods imported or exported (or attempted to be imported or exported) in violation of Section 11 are liable to confiscation. Copies of Sections 11 and 111 of the Customs Act 1962 are attached as Exhibit US-17. The complete act is available through the website of the Indian Ministry of Finance, Department of Revenue, Central Board of Excise and Customs, at <http://www.cbec.gov.in/cae/customs/cs-acts-main.htm>.

(c) Section 11(1) of the FTDR Act prohibits imports or exports by any person except in accordance with the provisions of the Act, the rules and orders made thereunder and the Export and Import Policy in force at the time. Under section 11(2), when any person makes or abets or attempts to make any illegal import or export, he is liable to a monetary penalty. Section 11(4) -- the section to which India draws attention -- provides that the IEC Number of the person concerned may be suspended if he fails to pay such a penalty. Under section 11(5), the goods concerned (together with any package, covering or receptacle and any conveyances) are liable to confiscation.

36. At the same time, India has also confirmed [redacted].[26] The *Foreign Trade (Regulation) Rules, 1993* were issued under the authority of section 19 of the FTDR Act, and a copy is attached as Exhibit US-18.

5. India Has Succeeded in Having Car Manufacturers Sign MOU's

37. All or virtually all companies manufacturing automobiles in India have signed an MOU in accordance with the standard format.[27]

38. In reply to written questions from Japan, India confirmed on 10 September 1998 that "the MOU's signed so far are in tune with the Public Notice No. 60" and that "the only factor influencing the signing of the MOU is whether the MOU draft submitted by the concerned company is in consonance with Public Notice No. 60."[28] On 14 September 1998 the Indian delegate informed the Committee on Trade-Related Investment Measures that "almost all the major car manufacturers had now signed MOU's."[29]

39. The Indian business press has also reported on the signing of MOU's. *See, e.g.*, "Maruti Inks Pact with DGFT to Import Kits for New Models", *The Financial Express*, August 10, 1998 (announcing the signature of an MOU by Maruti Udyog); "Mahindra Ford India, DGFT sign MOU," *The Indian Express*, Sept. 12, 1998 (in addition to Mahindra Ford India, the article lists Honda Siel Cars India, Fiat India Automobiles, Daewoo Motors India, and Mercedes Benz India as MOU signatories); "Executive Briefing: General Motors Signs MOU with DGFT," *The Financial Express*, December 17, 1998 (the article notes that General Motors India Ltd. has become the eighth car-maker to sign the document); "Toyota-Kirloskar, DGFT to Sign Pact", *The*

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[26] India's Answers to Questions by the United States, 13 July 2000, answer to supplemental question 3 (emphasis added); Exhibit US-11.

[27] The Government of India has advised the United States that "[redacted]" companies manufacturing passenger cars may not have signed an MOU because they do not seek to import CKD/SKD kits and components. India's Answers to Questions by the United States, 13 July 2000, answer to question 13; Exhibit US-11.

[28] *Replies by India to Questions Posed by Japan*, G/TRIMS/W/15, dated 10 September 1998 and circulated 30 October 1998, answers to questions 8 and 9; Exhibit US-5.

[29] *Committee on Trade-Related Investment Measures: Minutes of the Meeting Held on 14 September 1998*, G/TRIMS/M/9, circulated on 13 January 1999, para. 34 (attached as Exhibit US-25).

Financial Express, July 8, 1999 (announcing that Toyota Kirloskar Motors Pvt Ltd is "all set to ink" the MOU, which "would be signed by the month-end").[30]

40. It is easy to see why these companies have signed MOU's. India has stated clearly the consequences of failing to sign: "Companies shall not be granted an import license for CKD/SKD kits until a revised MOU is signed with the Government of India."[31] Because such kits and components cannot be imported into India without a license, this policy effectively prohibits any company from importing CKD/SKD kits and components unless it abides by the terms and conditions of Public Notice No. 60 and the MOU.

B. The Indian Automotive Sector: Foreign Investment in Manufacturing Opens Up But Is Accompanied by Protection for the Parts and Components Industry

41. According to the report that the WTO Secretariat prepared for the 1998 Trade Policy Review of India,[32] India's automobile manufacturing sector was initially developed under conditions of strong licensing regulations and restrictions on both imports and investment. Foreign investment was effectively banned and foreign technology transfers were subject to government approval. Any capacity expansion was restricted and required licences issued by the Government. One joint venture had been approved in 1983, however, between Maruti Udyog Limited (in which the Government of India has a large equity stake) and Japan's Suzuki Limited. This allowed the first multinational into the Indian automobile sector and resulted in the production of small, low-cost automobiles in India. Nevertheless, as of 1994 India still had only 28 vehicles per 1,000 people.

42. In 1993 the Indian car manufacturing industry was opened to foreign investment. Foreign equity participation was initially allowed up to 51%. The limit was later raised so that while permission up to 51% foreign equity participation is granted automatically, up to 100% foreign equity participation is also allowed if approved by the Foreign Investment Promotion Board.

43. Since then, there has been a high rate of foreign investment in the sector, with major international car manufacturers entering the market in the 1990's. The total amount of foreign direct investment (FDI) approved by the Government between August 1991 and end-December 1996 for passenger car manufacturing alone amounted to 22 billion Rupees (Rs), around 2.3 per cent of the total amount of FDI approved in India during this period. Although the option of setting up wholly-owned subsidiaries in India is now open to foreign companies, most have

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[30] These articles have been obtained from the website of the *Indian Express*, <www.expressindia.com> and are attached as Exhibit US-19.

[31] *Replies by India to Questions Posed by Japan*, G/TRIMS/W/15, dated 10 September 1998 and circulated 30 October 1998, answer to question 11; Exhibit US-5.

[32] *Trade Policy Review, India: Report by the Secretariat*, WT/TPR/S/33, 5 March 1998, Part IV, paras. 101-109.

preferred to establish joint ventures with Indian manufacturers. As of March 1998, the Secretariat had identified 17 approved joint ventures in India.[33]

44. The Secretariat's report also provided information on motor vehicle production and sales in India. Passenger car production in India rose from 260,000 million units in 1994/95 to 330,000 in 1995/96 and 410,000 in 1996/97.[34] Since the publication of the Secretariat's report, the Association of Indian Automobile Manufacturers has published additional statistics on vehicle production and new vehicle sales in India for 1998 and 1999. According to those data, more than 370,000 passenger vehicles were produced in India in 1998, and more than 585,000 cars in 1999. New vehicle sales rose from more than 390,000 in 1998 to more than 520,000 in 1999.[35]

45. With respect to automotive components (such as engine parts, electrical parts, transmission and steering parts, suspension and brake parts, equipment and other parts), the Secretariat's report for the Indian TPR noted that the value of their production rose from Rs 33.6 million in 1990/91 to Rs 67.5 billion by 1994/95 and Rs 91 billion in 1995/96. In 1994/95, auto component imports into India amounted to $415.7 million, and exports from India amounted to $471.5 million. In 1995/96, auto components imports reached $618.1 million, while exports rose to $586.6 million.[36]

46. The Secretariat's report noted that the Indian authorities estimated the level of indigenisation in the automobile components sector at around 90%. The Report also noted divergent views on the reason for this high level: According to the Indian authorities, the relative dependence of the sector on export markets had encouraged firms to upgrade the quality of their products, and the level of indigenisation was largely due to the performance of, and high standards maintained by, the automotive components sector. The Secretariat, however, also noted reports questioning the productivity of the components industry and claiming that a number of foreign investors were bringing their own auto components subsidiaries into India to provide them with higher quality inputs.[37]

47. The Secretariat's report further pointed out that the high level of indigenisation was also due in part to the Phased Manufacturing Program, which had required firms to agree to a list of components that would progressively be "Indianized".[38] Indigenisation was also due in part to another previous requirement that companies investing in the automobile sector in India must agree to increase the level of indigenisation in their units within a certain period of time.[39]

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[33] *Id.*, Table IV.15.

[34] *Id.*, Table IV.14.

[35] *See* Exhibit US-20.

[36] *Trade Policy Review, India: Report by the Secretariat*, WT/TPR/S/33, 5 March 1998, Part IV, Table IV.14.

[37] *Id.*, para. 109, n. 91.

[38] The program was discontinued for new projects in 1991, and was made inapplicable to older projects in 1994. *Id.*, Part III, para. 89.

[39] *Id.*

48. Public Notice No. 60 and the MOU's thus continue an Indian tradition of governmental measures to nurture the domestic auto parts and components industry. Indeed, that was the very reason that Indian officials gave for the adoption of Public Notice No. 60: "The objective of the new policy is to encourage local production of auto-components and thus, bring in modern technology and develop this key segment, explain ministry officials."[40] Regrettably, however, India chose to advance that objective through trade restrictions. The text of Public Notice No. 60 drives the point home: "Thus, *all* joint venture manufacturers *shall enter into an MOU* with DGFT for import of CKD/SKD kits/components."[41] At the very moment when, thanks to the opening to FDI in the finished vehicle manufacturing sector, the demand within India for such parts and components would be growing, India decided to protect its domestic goods from import competition.

C. As a Result of the *India - QR's* Dispute, India is Committed to Eliminating Its Import Licensing Regime, But It Nevertheless Plans to Maintain Public Notice No. 60 and the MOU's

49. Indian import licensing restrictions were the subject of a previous dispute between the United States and India, *India - Quantitative Restrictions on Imports of Agricultural, Textile and Industrial Products* ("*India - QR's*"),[42] which concerned 2,714 Indian HS tariff line items that were either "restricted" or "canalized" (*i.e.*, items that only designated state trading enterprises were permitted to import). The 2,714 line items in question were those that India had notified to the Committee on Balance-of-Payments Restrictions in May of 1997 as subject to quantitative restrictions maintained under Article XVIII:B of the GATT 1994.[43] Those tariff line items included the tariff line items from HS Chapter 87 to which Public Notice No. 60 applies.[44] After the Panel and Appellate Body rejected India's claimed balance-of-payment justification, India and the United States reached an agreement for the phasing out of those restrictions. India, however, intends to maintain the trade-restrictive requirements in Public Notice No. 60 and the MOU's.

50. The issue in *India - QR's* was whether India was entitled to maintain import restrictions on those 2,714 items at all. India did not dispute that the measures were quantitative restrictions within the meaning of Article XI:1 of the GATT 1994. Instead, India asserted that those

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[40] "Car Makers Have to Sign New MOU's in Accordance with New Automobile Policy", *Business Standard*, December 11, 1997; Exhibit US-22.

[41] Public Notice No. 60, para. 2; Exhibit US-1.

[42] The Panel Report in that dispute, WT/DS90/R, and the Appellate Body Report upholding the Panel Report, WT/DS90/AB/R, were adopted by the Dispute Settlement Body on 22 September 1999.

[43] *Notification under Paragraph 9 of the Understanding on the Balance-of-Payments Provisions of the General Agreement on Tariffs and Trade 1994*, WT/BOP/N/24, 19 May 1997, Annex I, Part B; selected pages are attached as Exhibit US-8.

[44] *See, e.g.*, Sl. Nos. 2401 (tariff heading 870321.01) and 2404 (tariff heading 870321.04) in the *Notification under Paragraph 9 of the Understanding on the Balance-of-Payments Provisions of the General Agreement on Tariffs and Trade 1994*, WT/BOP/N/24, 19 May 1997; Exhibit US-8. The code "AUTO/BOP-XVIII:B" is used "When imports of passenger cars and automotive vehicles are permitted without a licence on fulfilment of conditions specified in a Public Notice issued in this behalf, and restrictions on imports through NAL [*i.e.*, non-automatic licensing] are otherwise maintained." *Id.*, page 117.

restrictions were justified by the balance-of-payments provisions of GATT Article XVIII:B.[45] The United States disagreed that Article XVIII:B justified the restrictions.

51. The *India - QR's* panel therefore examined whether India was entitled to maintain its restrictions in accordance with GATT Article XVIII:B. The Panel considered the evidence presented by both parties, as well as information received from the International Monetary Fund. In addition, the panel considered but rejected India's arguments with respect to Article XVIII:9 and 11;[46] the Note Ad Article XVIII:11;[47] and the proviso to Article XVIII:11.[48] On the basis of its factual findings and legal rulings, the Panel concluded that as of 18 November 1997 (the date the panel was established), India's quantitative restrictions violated Articles XI:1 and XVIII:11 of GATT 1994 and were not justified by Article XVIII:B; that the measures at issue, to the extent they applied to products subject to the Agreement on Agriculture, violated Article 4.2 of the Agreement on Agriculture; and that the measures at issue nullified or impaired the benefits of the United States under GATT 1994 and the Agreement on Agriculture.[49] The Panel recommended that the DSB request India to bring the measures at issue into conformity with its obligations under the WTO Agreement.[50]

52. India appealed several of the panel's findings and conclusions to the Appellate Body. The Appellate Body rejected India's claims, and upheld the Panel's recommendations.[51]

53. After the Panel and Appellate Body reports were adopted, India informed the DSB that it was India's intention to meet its WTO obligations and that India would require a reasonable period of time to comply with the DSB's recommendations and rulings. On 28 December 1999, pursuant to Article 21.3(b) of the DSU, India and the United States reached a mutual agreement with respect to the reasonable period of time for India's implementation of the DSB rulings and recommendations.[52] In relevant part, the agreement provides as follows:

> The Parties hereby mutually agree, pursuant to Article 21.3(b) of the Understanding on Rules and Procedures Governing the Settlement of Disputes, that the reasonable period of time shall finally expire on 1 April 2001, as follows:

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[45] Report of the Panel in *India - QR's*, WT/DS90/R, adopted 22 September 1999, para. 3.40.

[46] *Id.*, paras. 5.176 - 5.184.

[47] *Id.*, paras. 5.213-5.215.

[48] *Id.*, paras. 5.216-5.222.

[49] *Id.*, para. 6.1.

[50] *Id.*, para. 6.2.

[51] Report of the Appellate Body in *India - QR's*, WT/DS90/AB/R, adopted 22 September 1999, paras. 153-154.

[52] *India - Quantitative Restrictions on Imports of Agricultural, Textile and Industrial Products: Agreement under Article 21.3(b) of the DSU*, WT/DS90/15, circulated on 17 January 2000. A copy is attached as Exhibit US-9. It includes a listing of the 1,429 tariff line items (out of the original 2,714) on which India still maintained balance-of-payments restrictions as of that date.

(a) on or before 1 April 2000, India may notify to the United States a listing of up to but no more than 715 items of the 1,429 items on which India currently maintains quantitative restrictions, and with respect to the up to 715 items so notified, the reasonable period of time shall expire on 1 April 2001; and

(b) with respect to all the other items, the reasonable period of time shall expire on 1 April 2000.

54. On 1 April 2000, India notified to the United States 715 items with respect to which India wished the reasonable period of time to expire on 1 April 2001.[53] As mentioned in paragraph 20 above, 75 tariff line items relating to motor vehicles are included in that notification. The quantitative restrictions applicable to imports of those finished vehicles (and to CKD/SKD kits/components for such vehicles) therefore currently remain in place. As a result of the DSB's rulings and the agreement with the United States, however, India is obligated to remove the import restrictions maintained on those items for balance-of-payments purposes no later than April 1 of this year.

55. However, India does not intend to terminate the requirements of Public Notice No. 60 or the MOU's when it eliminates the balance-of-payments restrictions on imports of SKD/CKD kits and components on 1 April 2001. India has made this clear on several occasions.

56. For example, in July of last year -- several months after the U.S.-India agreement on removal of quantitative restrictions -- India told the United States that [redacted].[54]

57. In August, Indian Industry Ministry officials told the press that automobile manufacturers who have entered into MOU's with the Government in the past will have to honor all their commitments in terms of exports, localisation level, and minimum capital invested in the venture.[55]

58. Finally, India's Director-General of Foreign Trade himself has confirmed India's intentions. He gave an interview, which was published on 22 August 2000, discussing the Indian Government's plans for its auto policy after the removal of the balance-of-payments restrictions. In response to "domestic auto-ancillary units, who felt threatened by the removal of QR's [and] have appealed to the government to protect their interests", the Director-General "hinted that manufacturers using a large percentage of local components are likely to benefit from several

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[53] A copy of the Indian notification is attached as Exhibit US-21. This notification was later rectified with respect to a small number of items not relevant to this dispute.

[54] India's Answers to Questions by the United States, 13 July 2000, answers to supplemental questions 4 and 5 (emphasis added); Exhibit US-11.

[55] "Centre Plans Tariff Cover for Auto-Ancillary Units," *The Financial Express*, August 2, 2000, attached as Exhibit US-23.

incentives to be announced as part of the new policy."[56] He went on to discuss the status of the existing MOU's:

> The government says that all the export commitments in the MOU's signed up to now will have to be fulfilled. After April 1, 2001, no MOU's will be required. The car companies do not have to sign any more MOU's with the government in the post-QR period but the outstanding export commitment in the MOU's already signed will have to be completed.
>
> "Under all circumstances, the auto industry will have to fulfill the outstanding export commitments even after quantitative restrictions are removed," [the Director-General] said. "They can't get away with it."

IV. LEGAL ARGUMENT

59. The measures at issue in this dispute discriminate against imported automotive parts and components in a variety of ways. These measures also restrict or prohibit the importation of foreign automotive components into India. As a result, they are inconsistent with India's obligations under Article III:4 of the GATT 1994; Article XI:1 of the GATT 1994; and Articles 2.1 and 2.2 of the TRIMs Agreement.

A. The Measures Are Inconsistent with Article III:4 of the GATT 1994

60. Article III:4 of the GATT 1994 states the following:

> The products of the territory of any contracting party imported into the territory of any other contracting party shall be accorded treatment no less favorable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use. ...

61. The indigenisation obligation and the trade balancing obligation in Public Notice No. 60 and the MOU's are in plain contravention of Article III:4. First, they each constitute "regulations" or "requirements" that "affect" the sale, purchase, and use of imported and domestic automotive components and kits: India requires motor vehicle manufacturers to buy and use local rather than imported goods, and to discharge an export obligation tied to imported components that they buy or use, in order to be allowed to import SKD/CKD kits and components. Second, imported automotive components are "like" domestic automotive components. Third, the indigenisation obligation and the trade balancing obligation are openly discriminatory and thus

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[56] "India's New Automobiles Policy Will Protect Domestic Industry Using Tariffs, Officials Say," *BNA Daily Report for Executives*, August 22, 2000, attached as Exhibit US-24.

accord "less favorable treatment" to imported automotive components and kits, in two ways: Manufacturers can meet the local content obligation only by purchasing and using Indian parts and components instead of imported ones in their production of motor vehicles; and manufacturers can reduce the burden of the export requirement and preserve marketing flexibility for their finished products only by purchasing and using Indian parts and components rather than imported ones. The Indian measures therefore accord a competitive advantage to Indian goods.[57]

1. The Indigenisation and Trade Balancing Requirements Are "Regulations" or "Requirements" that "Affect" the Sale, Purchase or Use in India of Foreign and Domestic Parts and Components

62. To begin with, the measures at issue in this case constitute at least "regulations" or "requirements", as those terms in Article III:4 are ordinarily understood.[58]

63. First, Public Notice No. 60 states that it was adopted "in the exercise of the powers conferred under Paragraph 4.11 of the [Exim Policy]."[59] Paragraph 4.11 of the Exim Policy provides that the Director-General of Foreign Trade may "in any case or class of cases specify the procedure to be followed ... for the purpose of implementing the provisions of the [FTDR] Act, the rules and orders made thereunder, and this Policy. Such procedures shall be ... published by means of a Public Notice."[60] The ordinary meaning of "regulation" includes its use as a generic term for governmental measures that implement statutes and other domestic legal provisions.[61] The word "regulation" in Article III:4 thus encompasses Public Notice No. 60.

64. Second, Public Notice No. 60 regulates the conduct of manufacturing firms (they must meet local content and trade balancing targets) and the conduct of the Indian import licensing authorities (they may issue licenses for CKD/SKD components and kits if those targets are met).

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[57] This three-part analysis corresponds to the Appellate Body's recent restatement of the examination that Article III:4 calls for: "For a violation of Article III:4 to be established, three elements must be satisfied: that the imported and domestic products at issue are 'like products'; that the measure at issue is a 'law, regulation, or requirement affecting their internal sale, offering for sale, purchase, transportation, distribution, or use'; and that the imported products are accorded 'less favourable' treatment than that accorded to like domestic products." Appellate Body Report in *Korea -- Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS161/AB/R, WT/DS169/AB/R, adopted 10 January 2001, para. 133.

[58] As the Appellate Body has recognized, Article 3.2 of the DSU requires the Panel to refer to the fundamental rules of treaty interpretation reflected in the Vienna Convention of the Law of Treaties (opened for signature May 23, 1969) (the "Vienna Convention"). *See, e.g.*, Report of the Appellate Body in *Japan - Taxes on Alcoholic Beverages*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R ("*Japan - Taxes*"), adopted on 1 November 1996, page 10. Article 31(1) of the Vienna Convention provides that "[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose."

[59] Exhibit US-1, para. 1.

[60] Exhibit US-4, para. 4.11.

[61] *See, e.g.*, *Black's Law Dictionary* (7th edition 1999), which defines "regulation" as, *inter alia*, "... A rule or order, having legal force, issued by an administrative agency or a local government."

Public Notice No. 60 falls within the ordinary meaning of the term "regulation" for that reason as well.[62]

65. Third, Public Notice No. 60 and the MOU's both impose "requirements" on firms manufacturing passenger cars in India. As soon as a firm signs an MOU in the form prescribed by Public Notice No. 60, it is required to achieve 50% local content during the first three years of the MOU, and 70% before the end of the fifth year. The words of the MOU make this clear: "... the party *shall achieve* indigenisation of components up to a minimum of 50% in the third year or earlier ... ."[63] That firm is also required to export cars and auto components with an FOB value at least equal to the CIF value of their importations of CKD/SKD kits and components. Once again, the words of the MOU are clear: "... the party *shall achieve* a broad neutralisation of foreign exchange in terms of balancing ..." exports and imports.[64]

66. Previous panels have considered similar situations. In the *FIRA* report, the panel recognized that the term "requirements" in Article III:4 properly described legally enforceable undertakings (*i.e.,* contractual commitments) given to the Government of Canada by individual companies:

> The Panel further noted that written purchase undertakings -- leaving aside the manner in which they may have been arrived at (voluntary submission, encouragement, negotiation, etc.) -- once they were accepted, became part of the conditions under which the investment proposals were approved, in which case compliance could be legally enforced. The Panel therefore found that the word "requirements" as used in Article III:4 could be considered a proper description of existing undertakings.[65]

67. In this case, as in *FIRA*, once the MOU's are approved by the Indian Government, the local content and trade balancing commitments in them become part of the conditions under which the MOU signatories are permitted to receive import licenses. India clearly means for those conditions to be enforced: "The MOU Scheme would be enforced through the import licensing mechanism and MOU signing firms would be granted import licenses by DGFT based on the progress made in respect of the parameters mentioned at para. III above."[66] And, as India has confirmed to the United States, [redacted].[67]

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[62] *See, e.g., The New Shorter Oxford English Dictionary* (3d edition, 1993), which defines "regulation" as, *inter alia*, ".... a rule prescribed for controlling some matter, or for the regulating of conduct; an authoritative direction, a standing rule".

[63] MOU, Paragraph III, clause (iv) (emphasis added); Exhibit US-1.

[64] MOU, Paragraph III, clause (vi) (emphasis added); Exhibit US-1.

[65] Panel Report in *Canada - Administration of the Foreign Investment Review Act ("FIRA")*, L/5504, adopted on 7 February 1984, BISD 30S/140, para. 5.4.

[66] MOU, Paragraph V. Exhibit US-1.

[67] India's Answers to Questions by the United States, 13 July 2000, answer to question 4; Exhibit US-11.

68. The analysis is not affected by the fact that manufacturing firms could in theory choose not to sign an MOU. Any firm that did so would forfeit the right to import CKD/SKD components and kits. Accepting the terms of an MOU, and complying with the indigenisation and trade balancing obligations in the MOU, are requirements that a firm must fulfill to obtain the right to import those kits and components. The term "requirement", in its ordinary meaning, encompasses such preconditions to obtaining a benefit from the government. *See, e.g., The New Shorter Oxford English Dictionary* (3d edition, 1993), which defines "requirement" as, *inter alia*, "Something called for or demanded; *a condition* which must be complied with."[68]

69. Previous panels have addressed this issue as well and have reached the same conclusion. For instance, in the *EEC -- Parts and Components* report, the panel recognized that requirements that an enterprise voluntarily accepts to gain government-provided advantages are nonetheless "requirements":

> The Panel noted that Article III:4 refers to "all laws, regulations or requirements affecting (the) internal sale, offering for sale, purchase, transportation, distribution or use." The Panel considered that the comprehensive coverage of "*all* laws, regulations or requirements *affecting*" the internal sale, etc. of imported products suggests that not only requirements which an enterprise is legally bound to carry out, ... but also those which an enterprise voluntarily accepts in order to obtain an advantage from the government constitute "requirements" within the meaning of that provision ... .[69]

70. The same analysis applies here. Car manufacturers in India that want to take advantage of the opportunity to import SKD/CKD kits and components must satisfy the local content and trade balancing obligations of Public Notice No. 60 and the MOU's. Public Notice No. 60 is unequivocal: "Thus, all joint venture manufacturers shall enter into an MOU with DGFT for import of CKD/SKD kits/components."[70]

71. In summary, the indigenisation and trade balancing obligations in Public Notice No. 60 and the MOU's are requirements -- and regulations -- within the meaning of Article III:4.

72. The measures' local content and trade balancing provisions also "affect" the sale, purchase and use of automotive parts and components. Ever since the *Italian Agricultural Machinery* report, panels have recognized that the term "affecting" in Article III:4 has a broad meaning, which extends not only to laws and regulations which directly govern the conditions of sale or

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[68] Emphasis added. That dictionary entry also offers the following example, in which the word "requirement" is used in this sense of precondition to receipt of an advantage or benefit: "To satisfy the college entrance requirements."

[69] Report of the Panel in *EEC - Regulation on Imports of Parts and Components ("EEC -- Parts and Components")*, L/6657, adopted on 16 May 1990, BISD 37S/132, 197, para. 5.21 (emphasis in original). *See also* the Report of the Panel in *Canada - Certain Measures Affecting the Automotive Industry ("Canada - Autos")*, WT/DS139/R, WT/DS142/R, adopted as modified by the Appellate Body with respect to other findings on 19 June 2000, para. 10.73.

[70] Public Notice No. 60, paragraph 2; Exhibit US-1.

purchase but also to any laws or regulations which might adversely modify the conditions of competition between the domestic and imported products on the internal market.[71]

73. The particular measures at issue here "affect" the sale, etc., of domestic and imported goods, because they require manufacturers in India to increase their purchases and use of Indian-made automotive parts and components at the expense of like foreign parts and components. A company manufacturing cars in India simply cannot import SKD/CKD kits and components unless it uses an increasing percentage of domestic goods (and therefore a decreasing percentage of imported goods) in its production -- 50% in the first three years, 70% by the fifth year. Moreover, the more a car manufacturer buys or uses imported kits and components, the more it has an obligation to allocate a portion of its output to export (regardless of its business preferences). In other words, the less a car manufacturer uses imported kits and components, the more freedom it has to allocate its output between the domestic and export markets. Both of these requirements make it less attractive, to say the least, for a manufacturer to purchase or use imported parts and components.

74. These requirements thus directly affect the competitive conditions under which automotive parts and components are purchased and used by manufacturers. Therefore, these incentives "affect" the use, purchase and sale of domestic and imported goods in India.

2. The Indigenisation and Trade Balancing Requirements Affect "Like" Domestic and Imported Products

75. There obviously are hundreds, if not thousands, of individual parts that go into a finished automobile. For purposes of Article III:4, however, imported automotive parts and components are "like" automotive parts and components made in India. Domestic and imported components to be used in manufacturing a particular car share the same physical characteristics and commercial uses. Thus, while a clutch and a shock absorber differ from each other, a domestic clutch and an imported clutch to be incorporated in a particular car are "like" each other, just as a domestic shock absorber and an imported shock absorber to be incorporated into a particular car are "like" each other. In India, however, the Government discriminates against the imported

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[71] Panel Report on *Italian Discrimination Against Imported Agricultural Machinery*, L/833, adopted 23 October 1958, BISD 7S/60, para. 12 ("[T]he text of paragraph 4 [of GATT Article III] referred ... to laws and regulations and requirements *affecting* internal sale, purchase, etc., and not to laws, regulations and requirements governing the conditions of sale or purchase. The selection of the word 'affecting' would imply, in the opinion of the Panel, that the drafters of the Article intended to cover in paragraph 4 not only the laws and regulations which directly governed the conditions of sale or purchase but also any laws or regulations which might adversely modify the conditions of competition between the domestic and imported products on the internal market.") (emphasis in original). *See also* Report of the Appellate Body in *European Communities - Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/AB/R, adopted 25 September 1997, para. 220 ("The ordinary meaning of the word 'affecting' implies a measure that has 'an effect on', which indicates a broad scope of application. This interpretation is further reinforced by the conclusions of previous panels that the term 'affecting' in the context of Article III of the GATT is wider in scope than such terms as 'regulating' or 'governing'.").

clutch, the imported shock absorber, and all other imported automotive parts and components, through measures that favor the purchase and use of their domestic counterparts.

3. The Indigenisation and Trade Balancing Requirements Discriminate Against Imported Parts and Components and Therefore Accord "Less Favourable" Treatment to Imported Products

76. The third step in the analysis requires an examination whether India's measures accord less favorable treatment to imported goods than to like domestic goods. The Appellate Body has recently reconfirmed the meaning of the phrase "treatment no less favourable":

> According "treatment no less favourable" means, as we have previously said, according *conditions of competition* no less favourable to the imported product than to the like domestic product.[72]

77. Applying that standard, each of these measures accords manifestly less favorable treatment to imported automotive parts and components in comparison to their domestically-made counterparts. Each of these measures places imported goods at a competitive disadvantage by creating conditions under which motor vehicle manufacturers operating in India have an incentive to use Indian-made parts or components. However, while the indigenisation requirement and the trade balancing requirement both discriminate against imported goods, they do so in slightly different ways.

Indigenisation

78. The indigenisation obligation of Public Notice No. 60 and the MOU's requires that car manufacturers "shall achieve indigenisation of components up to a minimum level of 50% in the third year or earlier from the date of clearance of first import consignment of CKD/SKD kits and 70% in the fifth year or earlier."[73] In fact, the MOU dictates that manufacturers "shall aggressively pursue and achieve *as soon as possible* the development of the local supply base".[74]

79. Car manufacturers therefore must rapidly decrease their use of imported components and parts. By the end of the third year, their production of finished vehicles can consist of 50%, 60%, or more Indian-origin parts; but, by governmental fiat, that same production can include no more than 50% foreign-origin parts and components. By the end of the fifth year, the situation for imported parts has deteriorated further: Indian-origin parts and components can comprise 70%, 80%, or more of a firm's production; but now, by governmental fiat, that same firm's production

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[72] Appellate Body Report in *Korea -- Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS161/AB/R, WT/DS169/AB/R, adopted 10 January 2001, para. 135 (emphasis in original) (citing Appellate Body Report in *Japan - Taxes*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, pages 16-17).

[73] Public Notice No. 60, para. 3(iii), and MOU, paragraph III, clause (iv); Exhibit US-1.

[74] MOU, paragraph III, clause (iv) (emphasis added); Exhibit US-1.

can include no more than 30% imported parts and components. The advantage that the indigenisation requirement gives to Indian goods is clear: their imported counterparts are simply not permitted to compete for the percentage of production that India expressly reserves for domestic goods.

80. Local content requirements such as this one have been systematically condemned by previous panels. In the *FIRA* dispute, for example, the panel considered undertakings to purchase goods of domestic origin. The panel had no difficulty recognizing that undertakings that excluded the possibility of purchasing available imported products clearly treated such imported products less favorably than domestic products, and that such requirements were therefore not consistent with Article III:4.[75]

81. It bears emphasizing that the indigenisation requirement disadvantages a broad class of foreign goods -- broader, in fact, than just kits and components imported in SKD/CKD form. The requirement discriminates against *any* imported part or component, from *any* non-Indian origin, that an Indian firm might use in manufacturing a motor vehicle. Any such foreign component, no matter how small or how separate from other parts, counts against a manufacturer trying to reach the mandated local content percentage. The discrimination in the measures' indigenisation requirement thus affects the conditions of competition of *all* such imported parts and components, and therefore accords imported parts and components treatment less favorable than it accords to like domestic items.

Trade balancing

82. The trade balancing requirement also modifies conditions of competition in favor of Indian goods, but its discrimination affects those parts and components that are imported in SKD or CKD form. The discrimination arises because the trade balancing requirement attaches an obligation to the purchase, sale and use of those imported kits and components that is not attached to like domestic goods.

83. Under Public Notice No. 60 and the MOU's, all imported SKD/CKD kits/components carry with them an obligation to export from India goods (components or finished vehicles) in a value equal to the value of the imported goods.[76] Moreover, this obligation attaches not only to

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[75] *FIRA*, para. 5.8. To the same effect is the Panel Report in *EEC -- Parts and Components:* "The Panel noted that the EEC made the grant of an advantage, namely the suspension of proceedings under the anti-circumvention provision, dependent on undertakings to limit the use of parts or materials of Japanese origin without imposing similar limitations on the use of like products of EEC or other origin, hence dependent on undertakings to accord treatment to imported products less favourable than that accorded to like products of national origin in respect of their internal use. The Panel therefore concluded that the decisions of the EEC to suspend proceedings ... conditional on undertakings by enterprises in the EEC to limit the use of parts or materials originating in Japan in their assembly or production operations are inconsistent with Article III:4." *EEC -- Parts and Components*, para. 5.21.

[76] Public Notice No. 60, paragraph 3(iv); MOU, paragraph III, clause (vi). The value of an importation is (continued...)

SKD/CKD kits/components that the manufacturer itself imports, but also to those SKD/CKD kits or components that the manufacturer purchases within India but were imported by someone else.[77] Domestic goods, on the other hand, are free of this obligation.

84. Consequently, each time a manufacturer decides whether to use imported SKD/CKD components rather than like domestic components, it must factor into its decision the export obligation that it will incur if it chooses imported rather than Indian components. If the manufacturer builds a car with components imported in SKD/CKD form, the manufacturer must either export that car or, if it wishes to sell that car on the Indian market, the manufacturer must export some other finished vehicle or auto components whose value equals that of the SKD/CKD importation. If, instead, the manufacturer builds that same car without using components imported in SKD/CKD form, the manufacturer is free to sell the car in whatever market it chooses; and, if the manufacturer chooses the domestic market, it does not have any export obligation to discharge. In short, the trade balancing requirement adds a burden to imported goods -- an interference with the distribution and other commercial choices of their user or purchaser -- that does not apply to like domestic goods. That additional burden is a disincentive to the use of imported SKD/CKD kits and components, and it therefore accords less favorable treatment to them.

85. A similar situation was considered in *EEC - Measures on Animal Feed Proteins*.[78] The measures examined in that case obligated importers of corn gluten feeds into the EEC to purchase a certain quantity of skimmed milk powder held by intervention agencies and to have it denatured for use as feed for animals other than calves.[79] Users of domestic corn gluten feeds did not have such an obligation. The panel was not convinced that the economic justifications put forward by the EEC justified the non-application of those measures to domestic corn gluten, and the panel therefore concluded that the measures accorded imported corn gluten less favorable treatment than that accorded corn gluten of national origin in violation of Article III:4.[80] The present dispute, like *Animal Feed Proteins*, involves a measure that imposes a burden on those who use imported goods but not on those who use like domestic goods (the obligation to buy milk powder from intervention agencies in that case, the obligation to export finished vehicles or auto parts in

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[76] (...continued)
determined by the value indicated on the import license. That value is given in both Rupees and freely convertible currency. The export obligation must be discharged in freely convertible currency, however. *Handbook of Procedures, Volumes 1 & 2* (the "Handbook"), para. 15.6. The Handbook, issued by the Ministry of Commerce, elaborates upon and supplements the general rules set forth in the Exim Policy. Chapters 1 through 5 and 15 of the Handbook are attached as Exhibit US-15 to this submission.

[77] India has confirmed that the trade balancing obligation "*includes the purchases in India* of the imported components or CKD/SKD kits." *Replies by India to Questions Posed by Japan*, G/TRIMS/W/15, circulated 30 October 1998, answer to question 23 (emphasis added); Exhibit US-5.

[78] Report of the Panel in *EEC -- Measures on Animal Feed Proteins*, L/4599, adopted on 14 March 1978, BISD 25S/49.

[79] *Id.*, para. 2.5.

[80] *Id.*, para. 4.10.

this one). As the *Animal Feed Proteins* recognized, such a measure is inconsistent with Article III:4.

86. In summary, Public Notice No. 60 and the MOU's are regulations or requirements that affect domestic and imported goods, and that treat imported goods less favorably than like domestic ones. Both the indigenisation requirement and the trade balancing requirement discriminate against imported parts and components in favor of their Indian counterparts. Indeed, these measures favor those "domestic auto-ancillary units, who [feel] threatened by the removal of QR's [and] have appealed to the government to protect their interests".[81] Public Notice No. 60 and the MOU's constitute precisely the type of protectionist regulatory measures that Article III:4 condemns.

B. The Measures Are Inconsistent with Article XI:1 of the GATT 1994

87. The indigenisation and trade balancing requirements in Public Notice No. 60 and the MOU's are also inconsistent with India's obligations under Article XI:1 of the GATT 1994, which provides as follows:

> No prohibitions or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licenses or other measures, shall be instituted or maintained by any contracting party on the importation of any product of the territory of any other contracting party ... .

88. The indigenisation and trade balancing requirements are "prohibitions or restrictions ... on ... importation", as those terms are used in Article XI:1. That operative phrase has a broad reach, and the measures in this case -- which on their face limit imports by manufacturers who do not meet those requirements -- clearly fall within it.[82]

1. In Article XI:1, the Terms "Prohibition" and "Restriction" Are Given a Broad Scope

89. As the panel on *Japan -- Trade in Semi-Conductors* pointed out, "this wording [of Article XI:1] was comprehensive; it applied to all measures instituted or maintained by a contracting party prohibiting or restricting the importation, exportation or sale for export of products other

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[81] "India's New Automobiles Policy Will Protect Domestic Industry Using Tariffs, Officials Say," *BNA Daily Report for Executives*, August 22, 2000, attached as Exhibit US-24.

[82] The United States also reserves all its rights with respect to the recommendations and rulings of the DSB in *India-QR's*. Inasmuch as the panel in that dispute found India's import licensing regime to be inconsistent with Article XI:1 (*see* paragraph 51 above), retention of non-automatic import licensing for motor vehicles or automotive parts and components beyond April 1, 2001 (including for the purpose of enforcing any of the MOU's requirements) would in any case be inconsistent with India's obligations under the DSU in that dispute. This part IV.B explains why the indigenisation and trade balancing requirements of Public Notice No. 60 and the MOU's are in themselves inconsistent with Article XI:1.

than measures that take the form of duties, taxes or other charges."[83] Similarly, the panel report in *EC -- Regime for the Importation, Sale and Distribution of Bananas* recognized that "past GATT panel reports support giving the term 'restriction' [in Article XI:1] an expansive interpretation."[84]

90. Outright prohibitions are clearly within the scope of Article XI:1. Thus, for example, the panel in *EEC - Programme of Minimum Import Prices, Licences and Surety Deposits for Certain Processed Fruits and Vegetables* found that a system that did not allow imports below a certain minimum price level constituted a "restriction other than duties, taxes or other charges " within the meaning of Article XI:1.[85]

91. However, discretionary or non-automatic import licensing by itself also constitutes a quantitative restriction on trade under Article XI:1, as the 1950 Working Party Report on a *Notification by Haiti under Article XVIII* recognized. Haiti had notified a law that, *inter alia*, provided for discretionary import licensing of imports of various tobacco products. The working party found that "in so far as the law establishing the Régie provided that the importation of tobacco, cigars and cigarettes should be subject to licences issued by a government authority and that licences should be issued at the discretion of that authority in the light of market requirements, there was an element of restriction in the measure which was contrary to Article XI of the General Agreement".[86]

92. Conditional suspensions of an import prohibition have also been considered inconsistent with Article XI:1. In the dispute concerning *Quantitative Restrictions Against Imports of Certain Products from Hong Kong,* the panel considered an import regime described as "a system which concerned imports of products subject in principle to quantitative restrictions but for which no quota amount had been set either in quantity or value, permit applications being granted on request. It could be defined as a suspension -- which was provisional and could be revoked at any time -- of strict quota limitation."[87] The panel found that that import regime would amount to a quantitative restriction within the meaning of Article XI unless it provided for the automatic issuance of licences.[88]

93. The panel in *India-QR's*, which examined the very licensing system that is currently used to enforce the measures at issue in this dispute, noted all of these precedents. It also pointed out

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[83] Panel Report on *Japan - Trade in Semiconductors*, L/6309, adopted on 4 May 1988, BISD 35S/116, para. 104.

[84] WT/DS27/R, adopted on 25 September 1997, para. 7.154.

[85] Panel Report on *EEC - Programme of Minimum Import Prices, Licences and Surety Deposits for Certain Processed Fruits and Vegetables*, L/4687, adopted on 18 October 1978, BISD 25S/68, para. 4.9.

[86] GATT/CP.5/25, adopted on 27 November 1950, BISD Vol. II/87.

[87] Panel Report on *Quantitative Restrictions Against Imports of Certain Products from Hong Kong*, L/5511, adopted on 12 July 1983, BISD 30S/129, para. 8.

[88] *Id.*, para. 31.

that the scope of the word "restriction" itself is broad, as seen in its ordinary meaning, which is "a limitation on action, a limiting condition or regulation."[89]

2. The Indigenisation and Trade Balancing Requirements Restrict or Prohibit Imports

94. The two obligations in Public Notice No. 60 and the MOU's each clearly fall within the extensive scope of Article XI:1 and constitute prohibitions or restrictions other than duties, etc., on the importation of SKD/CKD kits/components.

95. The indigenisation requirement is a straightforward restriction or prohibition on such imports. Failure to meet the 50% local content quota by the third year, or the 70% quota by the fifth year, leads to the denial of the right to import parts and components in SKD/CKD form. Public Notice No. 60 is clear about this: "... import of components for motor vehicle in CKD/SKD form ... shall be allowed for importation against a licence and *such a licence will be issued only* to joint venture automobile manufacturing companies *on the basis of an MOU* to be signed by those companies."[90] The MOU adds: "MOU signing firms would be granted import licenses by DGFT based on above parameters [*i.e.*, the MOU's substantive requirements, including indigenisation and trade balancing]"[91]; and "further licences will be issued to the party on the basis of an annual report of the progress made in relation to these parameters."[92] Moreover, India has confirmed that [redacted].[93]

96. Importantly, the indigenisation requirement (and the corresponding import restriction) is a continuing one. Public Notice No. 60 specifies no termination date for the MOU's. Relief from indigenisation-based import restrictions comes only to those who meet the local content target fully: "Once the MOU signing firm has reached an indigenisation level of 70%, there will be no need for further import licences from DGFT."[94] The implication is clear: as long as the indigenisation level is below 70%, imports are subject to restriction or prohibition.

97. The trade balancing requirement is likewise a continuing restriction on imports of SKD/CKD kits and components. The provisions of Public Notice No. 60 and the MOU mentioned in paragraph 95 apply to the trade balancing requirement as well. Moreover, paragraph 3(iv) of Public Notice No. 60 adds that "from 4th year onwards the value of imports may be regulated with reference to the export obligation fulfilled in the previous years as per the

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[89] Panel Report in *India-QR's*, WT/DS90/R, adopted 22 September 1999, para. 5.128 (quoting *The New Shorter Oxford Dictionary* (1993), page 2569).

[90] Public Notice No. 60, para. 2, Exhibit US-1. *See also Replies by India to Questions Posed by Japan*, G/TRIMS/W/15, circulated 30 October 1998, answer to question 11 (Exhibit US-5) ("Companies shall not be granted import licence for CKD/SKD kits until a revised MOU is signed with the Government of India.")

[91] Public Notice No. 60, para. 4, Exhibit US-1.

[92] MOU, paragraph IV, Exhibit US-1.

[93] India's Answers to Questions by the United States, 13 July 2000, answer to question 5, Exhibit US-11 (underlining in original, other emphasis added).

[94] Public Notice No. 60, para. 3(iii).

MOU." In other words, starting in the fourth year the MOU imposes a quantitative limitation on imports -- and the quantity is correlated to the degree of compliance with the trade balancing requirement.

98. The Government of India has confirmed that denial of an import license is effectively mandatory if the trade balancing obligation is not met. In response to a question from Japan about the consequences of failing to meet this obligation, India said: "CKD/SKD kits imports would be allowed with reference to the extent of export obligation fulfilled in the previous year. ... There is hardly any discretion involved in determining the extent of import of CKD/SKD kits except by way of considering any genuine problems the company may have faced in achieving the export levels."[95]

99. It is important to note that India asserts other means of restricting importations by MOU signatories besides denying licenses. A manufacturer's failure to comply with an MOU obligation can lead to loss of import privileges or to confiscation of the goods concerned pursuant to various provisions of the FTDR Act and the rules made thereunder:

[redacted][96]

100. These additional import-restricting provisions will evidently not disappear when India eliminates its balance-of-payments licenses on April 1, 2001, but will instead, apparently, become the instruments through which India carries out the import restrictions in Public Notice No. 60 and the MOU's (and thus prevents SKD/CKD kits/components from being brought into India to compete with domestic parts and components).

101. To be sure, the Indian authorities have on occasion asserted that Public Notice No. 60 and the MOU's were put in place to ensure transparency and objectivity in the administration of import licensing.[97] But that assertion misses the point: the fact that India has now adopted transparent and objective restrictions does not make them any less *restrictions*. A manufacturer that does not consent to Public Notice No. 60, or refuses to sign an MOU, or fails to adhere to the provisions of either, will be denied a license (or denied the right to import under provisions such as the FTDR Act) and will thus be restricted, or even prohibited, from importing.

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[95] *Replies by India to Questions Posed by Japan*, G/TRIMS/W/15, circulated 30 October 1998, answer to question 24; Exhibit US-5.

[96] India's Answers to Questions by the United States, answer to supplemental question 3; Exhibit US-11. Paragraph 35 above describes the provisions of the FTDR Act to which the Indian answer refers. Confiscation of the goods concerned is provided for both in section 3(3) of the FTDR Act (which permits confiscation pursuant to section 111 of the Customs Act 1962) and in section 11(5) of the FTDR Act. *See also*, India's Answers to Questions by the United States, 13 July 2000, answer to supplemental question 4; Exhibit US-11 ("[redacted]").

[97] For example, the Indian delegate told the Committee on Trade-Related Investment Measures that it "had therefore been felt necessary to evolve a mechanism by which these quantitative restrictions could be administered in a transparent and objective manner, and to obviate any subjective discretion in the sanction of licences. It was with this objective in mind that the policy regarding the conclusion of memorandums of understanding ('MOU') with car manufacturing firms had been formulated." *Committee on Trade-Related Investment Measures: Minutes of the Meeting Held on 14 September 1998*, G/TRIMS/M/9, para. 34.

Any restriction on imports other than duties, taxes or other charges violates Article XI:1; the fact that these measures may even *prohibit* imports of automotive components simply underlines the flagrant character of the violation in this case.

102. In fact, the import-restricting features of these measures complement their discriminatory features. They work together to advance India's goal of protecting its domestic parts and components industry. Not only do these measures discriminate in favor of domestic goods, as described earlier; they also ensure that competing foreign goods are kept out of India. Because of the discrimination, a manufacturer who achieves the local content and trade balancing quotas is permitted to import SKD/CKD kits and components; but that manufacturer will import at most the amount that is not reserved for Indian parts, namely 50% of production in the first three years, and no more than 30% of production by the fifth year. (The manufacturer will further limit its imports to an amount equivalent to the value of what it can expect to export.) Because of the import restrictions, a manufacturing firm that fails to achieve either quota will be denied licenses to import SKD/CKD kits/components altogether, and will therefore of course not even import the limited amounts imported by a compliant firm. In either case, the amount of parts and components entering India to compete with domestic parts and components is limited.

103. In summary, the indigenisation requirement and trade balancing requirement in Public Notice No. 60 and the MOU's fall within the category of restrictions that Article XI:1 forbids. As in *Quantitative Restrictions Against Imports of Certain Products from Hong Kong*, these measures amount to a provisional suspension of a strict import limitation (namely the ban on imports of CKD/SKD kits/components). But it is a suspension that is conditioned on continuing compliance with the indigenisation and trade balancing requirements, and that is able to be revoked whenever a manufacturing firm fails to meet either of them. These requirements are inconsistent with Article XI:1.

C. The Measures Are Inconsistent with Articles 2.1 and 2.2 of the TRIMs Agreement

104. As explained above, the indigenisation and trade balancing requirements of Public Notice No. 60 and the MOU's are inconsistent with India's obligations under Articles III:4 and XI:1 of the GATT 1994. They are also inconsistent with India's obligations under Articles 2.1 and 2.2 of the TRIMs Agreement.

1. The Relevant Provisions of the TRIMs Agreement

105. Article 2.1 sets out India's basic obligation, as follows:

> Without prejudice to other rights and obligations under GATT 1994, no Member shall apply any TRIM that is inconsistent with the provisions of Article III or Article XI of GATT 1994.

106. Article 2.2 provides for an illustrative list of trade-related investment measures that are inconsistent with two of the subparagraphs of Article III and Article XI of the GATT 1994, and therefore by definition inconsistent with Article 2.1:[98]

> An illustrative list of TRIMs that are inconsistent with the obligation of national treatment provided for in paragraph 4 of Article III of GATT 1994 and the obligation of general elimination of quantitative restrictions provided for in paragraph 1 of Article XI of GATT 1994 is contained in the Annex to this Agreement.

107. Paragraphs 1 and 2 of the illustrative list annexed to the Agreement (the "Illustrative List") provide in pertinent part as follows:

> 1. TRIMs that are inconsistent with the obligation of national treatment provided for in paragraph 4 of Article III of GATT 1994 include those which are mandatory or enforceable under domestic law or under administrative rulings, or compliance with which is necessary to obtain an advantage, and which require:
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> (a) the purchase or use by an enterprise of products of domestic origin or from any domestic source, whether specified in terms of particular products, in terms of volume or value of products, or in terms of a proportion of volume or value of its local production; or
>
> (b) that an enterprise's purchases or use of imported products be limited to an amount related to the volume or value of local products that it exports.
>
> 2. TRIMs that are inconsistent with the obligation of general elimination of quantitative restrictions provided for in paragraph 1 of Article XI of GATT 1994 include those which are mandatory or enforceable under domestic law or under administrative rulings, or compliance with which is necessary to obtain an advantage, and which restrict:

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[98] There are of course measures that are not contained in the Illustrative List but are nonetheless inconsistent with Article 2.1, for two reasons: First, the Illustrative List applies only to GATT Articles III:4 and XI:1, while the obligation in Article 2.1 extends to Article III and Article XI in general. Second, even with respect to Articles III:4 and XI:1, the list is only illustrative, not exhaustive; by its terms it does not limit the general rule of Article 2.1. On the first point, *see* Report of the Panel in *Indonesia - Certain Measures Affecting the Automobile Industry ("Indonesia-Autos")*, WT/DS54/R, WT/DS55/R, WT/DS59/R, WT/DS64/R, adopted 25 September 1997, para. 14.61. On the second point, *see* Report of the Panel in *Canada - Autos,* WT/DS139/R, WT/DS142/R, adopted as modified by the Appellate Body with respect to other issues on 19 June 2000, para. 10.89.

(a) the importation by an enterprise of products used in or related to its local production, generally or to an amount related to the volume or value of local production that it exports ... .

2. The Indigenisation and Trade Balancing Requirements are Inconsistent with TRIMs Agreement Articles 2.1 and 2.2

108. The indigenisation and trade balancing requirements of Public Notice No. 60 and the MOU's fall squarely within the scope of Paragraphs 1(a), 1(b) and 2(a) of the Illustrative List, and for that reason they are *per se* violations of Articles 2.1 and 2.2 of the TRIMs Agreement.

109. With respect to Paragraph 1(a), the indigenisation obligation is clearly a measure that "requires the purchase or use by an enterprise of products of domestic origin or from a domestic source". First, the firms manufacturing passenger cars in India are clearly "enterprises." Though the term is not defined in the TRIMs Agreement, the ordinary meaning of "enterprise" includes "a business firm, a company".[99] The manufacturers that are subject to Public Notice No. 60 and the MOU's come under that definition. Second, India has affirmed that [redacted];[100] and India's Director-General of Foreign Trade has specified that "for purposes of indigenisation, use of local materials alone will be taken into account ... . In other words, local value added will be the determining factor for arriving at the indigenisation level. If, however, no materials have been procured locally by a vendor, it will be construed as having failed to fulfill the norm."[101] Thus, the indigenisation provisions of Public Notice No. 60 and the MOU's require "enterprises" manufacturing automobiles to "use" local parts and components (and effectively also to "purchase" such local parts and components if they themselves do not import them). The indigenisation requirement therefore falls within the terms of Paragraph 1(a) of the Illustrative List.

110. With respect to Paragraph 1(b), the trade balancing obligation is a measure that "requires that an enterprise's ... use of imported products be limited to an amount related to the ... value of local products that it exports". Public Notice No. 60 and the MOU make clear that a signatory's imports of CKD/SKD "may be regulated with reference to the export obligation fulfilled in the previous years as per the MOU."[102] The export obligation itself is expressed in terms of value -- namely, an FOB value equal to the CIF value of imported CKD/SKD kits and components. Thus, while a firm manufacturing passenger cars in India may import SKD/CKD components that it wishes to use in its production, it can only import and use a maximum amount that is related to the value of its exports in previous years. Consequently, if such a firm wishes to use a greater amount of SKD/CKD components than that permitted maximum, it must purchase and use such

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[99] *The New Shorter Oxford English Dictionary* (3d edition, 1993).

[100] India's Replies to Questions Posed by the United States, 10 May 1999, answer to question 6; Exhibit US-14.

[101] "DGFT Open to Relaxation of Indigenisation Norms for Cars," *The Financial Express*, 12 January 1998, attached as Exhibit US-13.

[102] Public Notice No. 60, Paragraph 3(iv), Exhibit US-1.

components from an Indian source instead. The trade balancing obligation therefore falls within the terms of Paragraph 1(b) of the Illustrative List.

111. With respect to Paragraph 2(a), Public Notice No. 60 and the MOU's "restrict the importation by an enterprise of products used in or related to its local production", both "generally" and "to an amount related to the value of local production that it exports", in two ways. First, as described earlier, import licenses for SKD/CKD kits/components are not given to companies who do not sign an MOU and comply with its indigenisation and trade balancing requirements.[103] Because compliance with those requirements is a condition to importation of SKD/CKD kits/components (which are products such companies use in their motor vehicle production in India), those requirements "restrict" importation "generally" of "products used in ... local production". For that reason alone both the indigenisation requirement and the trade balancing requirement fall within the scope of Paragraph 2(a) of the Illustrative List.

112. The trade balancing obligation falls within the scope of Paragraph 2(a) for a second reason as well. According to the terms of Public Notice No. 60 and the MOU, a firm's import licenses for its CKD/SKD components are "regulated" with reference to the value of local production that the firm has exported (beginning in the fourth year of the MOU).[104] India expressed the restriction more directly in answering a question put by Japan: "CKD/SKD kits imports would be *allowed with reference to the extent of export obligation fulfilled* in the previous year."[105] Thus, the trade balancing obligation imposes a "restriction" on a firm's imports, and of course that restriction is "related to the ... value of local production that it [the firm] exports", as provided in Paragraph 2(a) of the Illustrative List.

113. In addition to falling within the specific terms of three subparagraphs of the Illustrative List, the measures also fall within the terms of the chapeaux to those subparagraphs. Paragraphs 1 and 2 both refer to measures which either are "mandatory or enforceable under domestic law or under administrative rulings" or "compliance with which is necessary to obtain an advantage." Public Notice No. 60 and the MOU's are such measures. First, India has confirmed several times that they and their requirements can be "enforced" at least under the provisions of the FTDR Act[106], through the import licensing mechanism and the Foreign Trade (Regulation) Rules 1993,[107] and [redacted].[108] Second, automobile manufacturers must comply with the indigenisation and trade balancing obligations in order to obtain permission to import SKD/CKD components and kits. Such permission constitutes an "advantage" inasmuch as it is not made available

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[103] *See, e.g.*, paragraphs 30-33 and 40 above.

[104] Public Notice No. 60, para. 3(iv), and MOU, paragraph III, clause (vi); Exhibit US-1.

[105] *Replies by India to Questions Posed by Japan*, G/TRIMS/W/15, circulated 30 October 1998, answer to question 24 (emphasis added); Exhibit US-5.

[106] *See, e.g., Replies by India to Questions Posed by Japan*, G/TRIMS/W/15, circulated 30 October 1998, answer to question 2 ("The Exim Policy and Public Notices are issued by the DGFT under the enabling provisions of the [FTDR] Act and are binding and legally enforceable.").

[107] *See* paragraph 36 above.

[108] India's Answers to Questions by the United States, 13 July 2000, answer to supplemental question 4; Exhibit US-11.

automatically -- components in SKD/CKD form are "restricted" items under the Exim Policy and not generally able to be imported into India.[109]

114. In summary, the measures at issue in this dispute fall under the Illustrative List. Pursuant to Article 2.2 of the TRIMs Agreement, therefore, they are TRIMs that are inconsistent with Articles III:4 and XI:1 of the GATT 1994. And, because they are TRIMs inconsistent with Articles III:4 and XI:1 of the GATT, they are therefore inconsistent with Article 2.1 of the TRIMs Agreement.

115. In addition, parts IV.A and IV.B of this submission demonstrated in detail how the indigenisation and trade balancing requirements of Public Notice No. 60 and the MOU's are inconsistent with Articles III:4 and XI:1 of the GATT 1994 in several respects. Therefore, to the extent that these measures discriminate against imported goods, or prohibit or restrict the importation of foreign goods, in ways that are not described in the provisions of the Illustrative List, the measures are nonetheless inconsistent with Article 2.1 of the TRIMs Agreement. For example, as described in paragraphs 82-85 above, the trade balancing requirement violates GATT Article III:4 because it imposes an obligation on users and purchasers of imported SKD/CKD parts and components -- namely, the obligation to export an equal value of automobiles or automotive components -- that it does not impose on users and purchasers of Indian parts and components. This form of discrimination may not be one of the kinds of inconsistency with Article III:4 included in Paragraph 1 of the Illustrative List and therefore may not be within the scope of Article 2.2 of the TRIMs Agreement. It is, however, nonetheless inconsistent with GATT Article III; and for that reason it is also inconsistent with Article 2.1 of the TRIMs Agreement.

3. These Measures are "Trade-Related Investment Measures"

116. It is not clear whether the TRIMs Agreement requires a separate analysis of whether a measure is a "trade-related investment measure". The panel in *Indonesia-Autos* declined to decide this question of interpretation because it considered that the measures in dispute were in any event trade-related investment measures.[110] In this case, whether or not the TRIMs

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[109] Two previous WTO panels have considered relief from otherwise applicable import duties as "advantages" to the importer: Report of the Panel in *Indonesia-Autos*, para. 14.89 (considering the matter specifically under the TRIMs Agreement), and Report of the Panel in *Canada - Certain Measures Affecting the Automotive Industry,* WT/DS139/R, WT/DS142/R, adopted as modified by the Appellate Body with respect to other issues on 19 June 2000, para. 10.90 (considering the issue in the context of GATT Article III:4). Relief from the otherwise applicable Indian import ban on SKD/CKD components/kits confers an analogous "advantage" to the importer.

[110] Report of the Panel in *Indonesia-Autos*, WT/DS54/R, WT/DS55/R, WT/DS59/R, WT/DS64/R, para. 14.71. In the view of the United States, any measure that falls within the scope of the Illustrative List is *per se* a trade-related investment measure. All measures on the Illustrative List involve "enterprises", and an enterprise is naturally the result of some investor's investment. Moreover, all measures on the Illustrative List are inconsistent with the obligation of national treatment in Article III:4 or the obligation of general elimination of quantitative restrictions in Article XI:1. Those obligations are central to the trading regime established under the GATT 1994

(continued...)

Agreement in fact demands a separate analysis of that question, the measures in this case definitely are "trade-related investment measures".

117. Public Notice No. 60 and the MOU's are clearly "investment measures", for several reasons. First, they require a minimum foreign equity of US $50 million dollars.[111] Such equity requirements are plainly devised to increase the inflow of foreign investment; under Public Notice No. 60 a company unwilling to invest that amount of foreign capital simply will not be allowed to sign an MOU and will not receive import licenses.

118. Second, Public Notice No. 60 and the MOU's attempt to steer foreign investment in the Indian motor vehicle manufacturing sector towards a particular kind of commercial and production structure. Those measures do so directly in paragraph 3(i) of Public Notice No. 60 (and paragraph III, clause (iii), of the MOU), which requires "establishment of actual production facilities for manufacture of cars and not for mere assembly of imported kits/components."[112] Indeed, India has confirmed that "the *purpose of the MOU is to encourage manufacture of cars as against mere import and re-assembly* of CKD/SKD kits that are restricted for imports due to balance of payments reasons."[113] India's measures also pursue this objective more subtly, by pressing manufacturers to use locally produced parts rather than importing SKD/CKD kits/components. As India explained in reply to a question about paragraph 3(i) of Public Notice No. 60, [redacted].[114]

119. Third, these measures are evidently aimed at encouraging investment in and the development of the Indian parts and components industry generally. The MOU makes that clear, because it provides that the manufacturing firm "shall aggressively pursue and achieve as soon as possible the development of the local supply base ... ."[115] Moreover, Indian officials announcing Public Notice No. 60 said that the policy objective was "to encourage local production of auto-components and thus, bring in modern technology and develop this key segment".[116] The indigenisation and trade balancing requirements further that objective both by skewing the competitive conditions in favor of local automotive parts and components and by restricting or even preventing the entry into India of foreign parts and components.

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[110] (...continued)
and for that reason are "trade-related".

[111] MOU, paragraph 3(ii), Exhibit US-1.

[112] *See also Replies by India to Questions Posed by Japan*, G/TRIMS/W/15, circulated 30 October 1998, answer to question 28: "Companies that create full manufacturing facilities are not required to sign the MOU's."

[113] *Replies by India to Questions Posed by Japan*, G/TRIMS/W/15, circulated 30 October 1998, answer to question 18 (emphasis added).

[114] India's Replies to Questions Posed by the United States, 10 May 1999, answer to question 4; Exhibit US-14.

[115] MOU, paragraph III, clause (iv); Exhibit US-1.

[116] "Car Makers Have to Sign New MOU's in Accordance with New Automobile Policy", *Business Standard*, December 11, 1997; Exhibit US-22.

120. In summary, Public Notice No. 60 and the MOU's constitute an attempt by India to encourage significant sums of foreign capital in one kind of investment (what it calls "manufacturing") and not another (what it considers "assembly"). Moreover, the indigenisation and trade balancing requirements are designed, first, to prod automobile companies in that direction by making it progressively harder for them to obtain and use imported kits, and, second, to enhance the development of India's domestic parts and components industry (from whom India plainly wants automobile companies to purchase the components and parts that they need to engage in "manufacture"). For all these reasons, the measures at issue are "investment" measures.

121. The measures are also clearly "trade-related". As already explained, they favor domestic goods over like imported goods, and they restrict or prohibit importation. With respect to local content requirements, the panel in *Indonesia-Autos* had no difficulty recognizing that such measures are trade-related by definition.[117] Quantitative import restrictions and prohibitions, the elimination of which is a cornerstone of the GATT 1994, are no less so. Indeed, past GATT panels have regarded violations of Article XI:1 in a special light because of the fundamentally trade-distorting nature of quantitative restrictions. For instance, the panel on *Japan - Restrictions on Imports of Certain Agricultural Products* found that "Article XI:1 protected expectations on competitive conditions . . . the presumption that a measure inconsistent with Article XI causes nullification or impairment could therefore not be refuted with arguments relating to export volumes."[118]

122. For these reasons, the measures at issue in this dispute are "trade-related investment measures".

4. India Cannot Claim the Benefits of the Transition Provisions in the TRIMs Agreement

123. Under Article 5.2 of the TRIMs Agreement, all WTO Members benefitted from a transition period to eliminate trade-related investment measures inconsistent with Article 2 of the Agreement. Those transition provisions, however, do not apply to the measures at issue in this case, for three reasons.

124. First, India introduced these measures in December of 1997, nearly three years after the entry into force of the WTO Agreement. Pursuant to Article 5.4 of the TRIMs Agreement, however, the transition provisions do not apply to measures adopted at that late date: "TRIMs introduced less than 180 days before the date of entry into force of the WTO Agreement shall not

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[117] Report of the Panel in *Indonesia-Autos*, para. 14.82.

[118] L/6253, adopted on 2 February 1988, BISD 35S/163, para. 5.4.3, citing also as support the Report of the Panel in *U.S. - Taxes on Petroleum and Certain Imported Substances*, L/6175, adopted on 17 June 1987, BISD 34S/136, and the Report of the Panel in *Japanese Measures on Imports of Leather*, in which the panel stated that it "wished to stress that the existence of a quantitative restriction should be presumed to cause nullification or impairment not only because of any effect it had had on the volume of trade but also for other reasons, *e.g.*, it would lead to increased transaction costs and would created uncertainties which could affect investment plans." L/5623, adopted on 15/16 May 1984, BISD 31S/94, para. 55.

benefit from the transitional arrangements provided in paragraph 2." For that reason alone, therefore, these measures were never entitled to any transition period and were inconsistent with India's obligations under the TRIMs Agreement on the day they were adopted.

125. Second, pursuant to Article 5.2 the only measures to which the transition provisions apply are those that were notified in accordance with the provisions of Article 5.1. India did notify the WTO in 1995 of a dividend balancing requirement in various sectors (*i.e.*, a firm will be allowed to repatriate dividends only to the extent that it has earned the necessary foreign exchange by exporting), including portions of the automotive sector.[119] India did not notify local content or trade balancing requirements, however, and the 1995 notification therefore has no effect on this case. Furthermore, in reply to a question posed by the United States, India confirmed that the requirements in Public Notice No. 60 and the MOU's do not fall within the scope of India's 1995 notification.[120]

126. Third, India's transition period for all TRIMs has in any case ended. Pursuant to Article 5.2 of the TRIMs Agreement, India had five years from the entry into force of the WTO Agreement to eliminate its trade-related investment measures. That five-year period expired on January 1, 2000. None of India's TRIMs -- whether notified or not -- can benefit from any further period of transition.

5. Conclusion

127. For all the foregoing reasons, India's measures -- Public Notice No. 60 and the MOU's, and the indigenisation and trade balancing requirements that they contain -- are inconsistent with Articles 2.1 and 2.2 of the TRIMs Agreement.

V. CONCLUSION

128. The United States respectfully requests that the Panel find that the measures at issue in this dispute are inconsistent with Articles Article III:4 and XI:1 of the GATT 1994 and Articles 2.1 and 2.2 of the TRIMs Agreement. The United States further requests that the Panel recommend that India bring its measures into conformity with its obligations under the GATT 1994 and the TRIMs Agreement.

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[119] *Notification under Article 5.1 of the Agreement on Trade-Related Investment Measures*, G/TRIMS/N/1/IND/1/Add.1, dated 22 December 1995 and circulated 16 January 1996, Exhibit US-26. Annexure I explains that India's dividend balancing requirement permits a firm to repatriate dividends only to the extent that it has earned the necessary foreign exchange by exporting. The United States reserves its position on whether this notification complied with Article 5.1.

[120] *Replies by India to Questions Posed by USA*, G/TRIMS/W/16, circulated 30 October 1998, answer to question 2 ("'Dividend balancing' provisions reflected in notification No. G/TRIMS/N/1/IND/1/Add.1 are explained in Annexure 1 to the notification. The policy for import of CKD/SKD kits by car manufacturers is not covered by this notification.").

INDIA -- MEASURES AFFECTING THE AUTOMOTIVE SECTOR
(WT/DS146-175)

U.S. EXHIBITS

No.	Description
1.	Public Notice No. 60 and the standard-form MOU
2.	U.S. consultation request, 2 June 1999 (circulated 7 June 1999 as document WT/DS175/1)
3.	U.S. panel request, 15 May 2000 (circulated 18 May 2000 as document WT/DS175/4)
4.	The Export and Import Policy 1 April 1997 - 31 March 2002, as amended through 13 October 2000, Chapters 1 through 5
5.	"Replies by India to Questions Posed by Japan," G/TRIMS/W/15, circulated 30 October 1998
6.	ITC (HS) Classifications of Export and Import Items (sample pages)
7.	"Replies to Questionnaire on Import Licensing Procedures," G/LIC/N/3/IND/4, circulated 4 December 2000
8.	"Notification under Paragraph 9 of the Understanding on the Balance-of-Payments Provisions of the General Agreement on Tariffs and Trade 1994," WT/BOP/N/24, 19 May 1997 (relevant pages)
9.	"India - Quantitative Restrictions on Imports of Agricultural, Textile and Industrial Products: Agreement under Article 21.3(b) of the DSU," WT/DS90/15, circulated on 17 January 2000
10.	ITC (HS) Import Licensing Note on SKD/CKD
11.	India's Answers to Questions by the United States, 13 July 2000
12.	Public Notice No. 3, dated 6 January 1998, issued by the Delhi Customs House
13.	"DGFT Open to Relaxation of Indigenisation Norms for Cars," *The Financial Express*, 12 January 1998
14.	India's Replies to Questions Posed by the United States, 10 May 1999
15.	The Handbook of Procedures, Volume 1, chapters 1 - 5 and 15
16.	The Foreign Trade (Development and Regulation) Act 1992
17.	Sections 11 and 111 of the Customs Act 1962 (and the table of contents of the Act)
18.	The Foreign Trade (Regulation) Rules, 1993

No.	Description
19.	Articles from the *Indian Express* and the *Financial Express* listing MOU signatories
20.	Indian Vehicle Production Data and New Vehicle Sales Data for 1998 and 1999 from the Association of Indian Automobile Manufacturers
21.	Indian notification to the United States under the U.S. – India BOP Settlement: Products To be Freed by 1 April 2001
22.	"Car Makers Have to Sign New MOU's in Accordance with New Automobile Policy", *Business Standard*, December 11, 1997
23.	"Centre Plans Tariff Cover for Auto-Ancillary Units," *The Financial Express*, August 2, 2000
24.	"India's New Automobiles Policy Will Protect Domestic Industry Using Tariffs, Officials Say," *BNA Daily Report for Executives*, August 22, 2000
25.	"Committee on Trade-Related Investment Measures: Minutes of the Meeting Held on 14 September 1998," G/TRIMS/M/9, circulated 13 January 1999
26.	"Notification under Article 5.1 of the Agreement on Trade-Related Investment Measures," G/TRIMS/N/1/IND/1/Add.1, circulated 16 January 1996